No. 00-631

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In The

Supreme Court of the United States

BENEDICTO V. YUJUICO, et al.,

Petitioners,

v.

FIRST PACIFIC BANK LIMITED,

Respondent.

On Petition For A Writ Of Certiorari To The California Court Of Appeal For The First Appellate District, Division Four

RESPONDENT'S BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

PAUL D. FOGEL
Counsel of Record
ANTHONY THEOPHILOS
MICHAEL E. DELEHUNT
RAYMOND A. CARDOZO
CROSBY, HEAFEY, ROACH & MAY
PROFESSIONAL CORPORATION
Two Embarcadero Center, Suite 2000
San Francisco, CA 94111
Telephone: (415) 543-8700
Facsimile: (415) 391-8269

Attorneys for Respondent
First Pacific Bank Limited

COCKLE LAW BRIEF PRINTING CO., (800) 225-6964
OR CALL COLLECT (402) 342-2831

QUESTION PRESENTED

Whether the California Court of Appeal's unpublished decision correctly affirmed the trial court's judgment of foreclosure, where Petitioners:

(1) To settle foreclosure litigation, stipulated to the entry of judgment for valuable consideration while represented by counsel;

(2) Thereafter sought to delay or avoid entry of judgment by manufacturing an arbitration demand that, after giving petitioners notice and the opportunity to be heard, the state courts found to be "wholly groundless";

(3) Raised no question arising under the Federal Arbitration Act until after the Court of Appeal issued its unpublished opinion; and

(4) Did not raise their present due process claim in the California Supreme Court.

CORPORATE DISCLOSURE STATEMENT

Pursuant to Rule 29.6, Respondent First Pacific Bank Limited represents that it is a foreign corporation owned 100 percent by FEB (1989) Limited, which in turn is owned 100 percent by FPB Bank Holding Company Limited, which in turn is owned 51 percent by FPMF Limited, 24 percent by MIMET FOTIC Investment Limited and 25 percent by the public. All of the above are foreign corporations, based either in Bermuda or in Hong Kong.

TABLE OF CONTENTS

		Page
I	PRELIMINARY STATEMENT	1
II	STATEMENT OF THE CASE	3
III	REASONS THE PETITION SHOULD BE DENIED	12
	A. Petitioners' Failure To Raise In A Timely And Proper Way In The State Courts The Issues They Are Raising In Their Petition Is Reason Alone For The Court To Deny Certiorari	13
	B. In Any Event, Neither Of The Issues Petitioners Raise Warrants This Court's Attention	15
	1. There Is No Conflict Between The California Supreme Court's *McCarroll* Decision And This Court's Precedents Concerning Arbitral Jurisdiction	15
	2. Even Though They Waived Their Due Process Rights, The Trial Court Gave Petitioners Full Due Process In Connection With Entry Of The Judgment, So There Is No Basis For Their Due Process Claim	24
IV	CONCLUSION	27

TABLE OF AUTHORITIES

Page

CASES

Allied-Bruce Terminix Cos. v. Dobson, 513 U.S. 265 (1995) 21

Bankers Life and Casualty Co. v. Crenshaw, 486 U.S. 71 (1988) 14

Clark v. Jeter, 486 U.S. 456 (1988) 14

D.H. Overmyer Co. v. Frick Co., 405 U.S. 174 (1972) 24

Dist. of Columbia Ct. of Appeals v. Feldman, 460 U.S. 462 (1983) 11

Drake Bakeries v. Bakery Workers, 370 U.S. 254 (1962) 9, 24

FRG, Inc. v. Manley, 919 F. 2d 850 (3d Cir. 1990) 25

First Options of Chicago v. Kaplan, 514 U.S. 938 (1995) 15

Hughes v. Blue Cross of N. Cal., 215 Cal. App. 3d 832 (1989) 13

ITT Hartford Life & Annuity Ins. Co. v. Amerishare Investors, Inc., 133 F. 3d 664 (8th Cir. 1998) 18

Int'l Union, United Auto. Aircraft v. Benton Harbor Malleable Ind., 242 F. 2d 536 (6th Cir. 1957) 17

In re Marriage of Jacobs, 128 Cal. App. 3d 273 (1982) 26

Local 205, United Elec., Radio & Mach. Workers of Am. v. Gen'l Elec. Co., 233 F. 2d 85 (1st Cir. 1957) 17

TABLE OF AUTHORITIES – Continued

Page

Local No. 358 Bakery & Confec., etc. v. Nolde Bros., Inc., 530 F. 2d 548 (4th Cir. 1975)..... 17

McCarroll v. L.A. County etc. Carpenters, 49 Cal. 2d 45 (1957)..... *passim*

New York ex rel. Bryant v. Zimmerman, 278 U.S. 63 (1928)..... 13

People v. Scott, 14 Cal. 4th 544 (1996)..... 13

Perry v. Thomas, 482 U.S. 483 (1987)..... 21

Portland Gen. Electric Co. v. U.S. Bank Trust Nat. Assoc., 218 F. 3d 1085 (9th Cir. 2000)..... 22

Rooker v. Fidelity Trust Co., 263 U.S. 413 (1923)..... 11

Rooney v. Inv. Co., 10 Cal. 3d 351 (1973)..... 25

Southland Corp. v. Keating, 465 U.S. 1 (1984)..... 21

United Steelworkers v. American Mfg. Co., 363 U.S. 564 (1960)..... 17

Webb v. Webb, 451 U.S. 493 (1981).....13, 14

Wright v. Universal Maritime Servs. Corp., 525 U.S. 70 (1998)..... 18

STATUTES

9 U.S.C. § 2..... *passim*

Cal. R. Ct. 977(a).....2, 12

Cal. R. Ct. 29(b)(1)..... 14

S. Ct. R. 10..... 12

TABLE OF AUTHORITIES – Continued

Page

S. Ct. R. 14.1(g)(i) 15

Cal. Civ. Code § 1638..... 16

Cal. Civ. Code § 1643..... 16

I

PRELIMINARY STATEMENT

Certiorari is reserved for cases that present groundbreaking issues of broad national significance that the petitioning party has properly raised in the courts below. This case does not fall into that category.

Petitioners have raised two issues for review: (1) whether the Federal Arbitration Act prevents a trial court from declining to refer a "wholly groundless" claim of arbitrability to arbitration; and (2) whether the entry of a stipulated judgment after petitioners waived their right to notice and an opportunity to object to its entry (and after petitioners participated in the entry-of-judgment procedure and were heard on their motion to vacate the judgment) violated due process. Neither issue is appropriate for review, for two reasons.

First, Petitioners failed to raise both of these issues in the state court proceedings in a timely and proper fashion, as this Court's decisions require. Petitioners did not raise their first issue until after the California Court of Appeal filed its opinion. And they did not raise their second issue when they sought review of that opinion in the California Supreme Court. Petitioners nowhere attempt to explain these failings because they cannot. These omissions alone are grounds for denying their petition.

Second, the Court of Appeal's unpublished opinion resolved questions of state law that do not implicate any important national policy, let alone federal questions of any significance. Petitioners are simply wrong in asserting otherwise.

Petitioners' first claim involves an invented conflict between California and federal law concerning a court's obligation to refer the arbitrability of a dispute to arbitration. In fact, the federal and state courts are in full accord on the rule that the Court of Appeal applied – that a trial court has the right, notwithstanding the Federal Arbitration Act, to perform a limited "gatekeeping" function and refuse to send to arbitration "wholly groundless" claims of arbitrability. It is not surprising that when Petitioners *did* raise this claim below (albeit belatedly), the lower courts rejected it. Thus, review would accomplish nothing because the lower courts were correct, and there is no conflict to resolve.

Petitioners' second claim involves a purported due process violation in the entry of a stipulated judgment. But while represented by the counsel of their choice, Petitioners waived their due process rights when they stipulated to the judgment. Even so, they were given notice and were heard – both before and after the judgment was entered. Petitioners were apparently satisfied with the Court of Appeal's rejection of their due process claim, as they failed to renew it when they sought California Supreme Court review.

The Court of Appeal's decision is of no interest to anyone except the parties involved in this dispute. Like all unpublished California Court of Appeal decisions, it may not be cited outside the confines of this case. *See* Cal. R. Ct. 977(a). Moreover, and because of Petitioners' procedural failings, the opinion does not even address one of the two purportedly compelling questions that Petitioners now assert.

At bottom, the petition is the latest of Petitioners' numerous maneuvers to undo the inevitable consequences of their default on a multi-million dollar commercial loan. At this point, all twelve state court jurists and the one federal judge who have examined this case have rejected Petitioners' claims. Justice O'Connor recently joined that list when she denied their application for a stay in No. 00-A286. This Court should see the matter likewise and deny the petition.

II

STATEMENT OF THE CASE

Respondent First Pacific Bank Limited (First Pacific) cautions the Court not to rely on Petitioners' Statement of the Case. (Petn. at 2-7) That is because Petitioners have omitted from it crucial facts as well as their own procedural failings that effectively doom their request for review. For example, while the Court of Appeal's holding was based on the premise that their claim of arbitrability was "wholly groundless," in their petition, Petitioners never explain the nature of the dispute they believe should have been arbitrated. Presumably, they have omitted that explanation because it would show that the state courts correctly rejected their argument. First Pacific therefore asks the Court to look to the state Court of Appeal's recitation of the facts and procedural history [P-App. A at 1-4][1] and the other of-record documents in the

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[1] We refer to Petitioners' Appendix as "P-App." and Respondent's Appendix as "R-App."

parties' appendices – matters that First Pacific summarizes below.

In 1989 and 1991, First Pacific issued a multi-million dollar commercial loan to Petitioners Benedicto Yujuico, Teresita Yujuico and the BVY Group, Inc. (P-App. A at 1-2) The loan was secured by real property in Atherton, California that Petitioners then owned. (*Id.*) After Petitioners defaulted on their payments, First Pacific filed a foreclosure action against them. (P-App. A at 2) Rather than pay the money they owed, Petitioners forced First Pacific to litigate its right to foreclosure. Finally, in August 1997, the parties entered into a settlement ("the Agreement") that restructured the terms of the loan. (*Id.*)

Under the Agreement, and in exchange for First Pacific's agreement to reduce Petitioners' debt by several million dollars to $5.2 million, Petitioners agreed to a new payment schedule. (*Id.*) The Agreement did not provide for nor discuss payment by third parties. (*Id.* at 1)

Attached to and made part of the Agreement were: (1) a stipulated Arbitral Award ("Award") that set Petitioners' liability to First Pacific at $7.5 million; (2) a Stipulation for Enforcement of the Award, and (3) a Stipulated Judgment against Petitioners ("Stipulation") with an attached Judgment of Foreclosure and Order of Sale ("Judgment"). (P-App. A at 2) The Award allowed for foreclosure on the Atherton property and stated that, in the event of any ensuing defaults in the payments, Petitioners waived several rights pertaining to the property, including the right to redeem it after foreclosure. (P-App. A at 2, B at 3)

As the Agreement showed on its face, the key consideration for First Pacific's substantial reduction in Petitioners' debt was Petitioners' promise that there would be no more delays in paying it off. Thus, the Agreement provided that if Petitioners failed to make a payment, First Pacific would be entitled to enforce the Award and obtain the Stipulated Judgment. (P-App. A at 2) First Pacific could avail itself of these remedies without notice to Petitioners. (*Id.*)

The Agreement also provided for arbitration of any dispute "relating to or arising out of [the] Agreement" through arbitration in San Francisco, under the authority of J.A.M.S./ENDISPUTE (a California-based alternative dispute resolution organization), "in accordance with the International Arbitration Rules of the American Arbitration Association." (*Id.* at 2) Article 15.1 of those rules states that "the tribunal shall have the power to rule on its own jurisdiction, including any objection to the existence, scope or validity of the arbitration agreement."

In February 1998, First Pacific agreed to an amendment that gave Petitioners an extended payment schedule. (P-App. A at 2)[2] They then made some of the required payments. However, on September 9, 1998, petitioner Benedicto Yujuico's father, Jesus Yujuico – who was not a party to the Agreement – offered to purchase First Pacific's right to payment of Petitioners' indebtedness ("the BVY Note") on an extended payment plan and

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[2] Jesus Yujuico, petitioner Benedicto Yujuico's father, signed a guarantee that was attached to the amendment. (P-App. A at 2) However, Jesus Yujuico was only a guarantor, not a party to the amendment or to the amended Agreement. (*Id.*)

under terms that the Agreement did not include. (P-App. A at 3)

This purchase offer was *not* a tender of performance of Petitioners' obligations under the Agreement, but an offer for a new agreement with new terms and new parties. Indeed, Jesus Yujuico's representative recognized in making the proposal that "[w]e realize that you can deny our request and instead foreclose the BVY Group collateral." (P-App. A at 3)

This "realization" represented a concession that would become significant in the proceedings that later arose: nothing in the Agreement or the amendment required First Pacific to accept a substitute debtor, to agree to sale of the BVY Note, or to accept altered payment terms – and Jesus Yujuico's purchase offer would have required all three. (P-App. A at 2-3) Furthermore, First Pacific did not particularly want to become involved with Jesus Yujuico and assume the risk that he might not abide by the proposed payment plan because he had previously been involved in litigation with First Pacific, arising out of loans to a corporation in which he had been the owner. (*Id.*)

Thus, on September 10, 1998 (five days before the due date for Petitioners' next payment), First Pacific advised Jesus Yujuico that it was rejecting his proposal. (*Id.*) September 15 then came and went without Petitioners making their required $450,000 payment. On September 16, First Pacific wrote Petitioners, advising them that it would invoke its rights under the Agreement. Petitioners still did not make the payment. Instead, Jesus Yujuico reiterated his offer to substitute a new contract on

altered terms. On September 17, First Pacific again rejected his offer. (P-App. A at 3-4)

On September 30, First Pacific again wrote Petitioners, stating it would invoke its right to perfect the Stipulated Judgment under the Agreement if it did not receive payment by October 5. (P-App. A at 4) Instead of making the payment, Petitioners demanded arbitration, alleging that they had "tendered" performance by submitting Jesus Yujuico's new purchase offer. (*Id.*) First Pacific then informed Petitioners that there was no basis for arbitration – after all, the offer did not give rise to a dispute that "related to or arose out of the Agreement" – and that it would seek the remedies that the Agreement permitted. (*Id.*)

On October 9, First Pacific filed an ex parte application for enforcement of the Award and entry of the Judgment in the San Mateo County Superior Court. (P-App. A at 4) Even though Petitioners had waived their right to notice in the Agreement, First Pacific gave them notice, and they appeared at the ex parte hearing to oppose entry of the Judgment. (*Id.* at 2, 4, 6) After determining that nothing in the Agreement obligated First Pacific to accept a third party offer of substitute performance, the trial court entered the judgment of foreclosure for First Pacific, as the Agreement permitted. (*Id.* at 4)

Thirty days later, Petitioners moved to vacate the judgment. After First Pacific filed opposition and Petitioners filed a reply, and after Petitioners failed to appear at a hearing at which they had the right to contest the court's "tentative ruling," the trial court denied Petitioners' motion. (*Id.* at 4; R-App. I) In none of Petitioners'

pleadings did they mention the Federal Arbitration Act [9 U.S.C. § 2 (FAA)], much less argue that the FAA governed the alleged "dispute" over arbitrability. (R-App. II-III)[3]

Petitioners then appealed the foreclosure judgment to the California Court of Appeal. In that appeal, they made the following arguments, all based on state law: (1) First Pacific's failure to comply with the arbitration provision of the Agreement deprived it of standing to seek entry of the stipulated judgment, and the arbitration provision deprived the trial court of jurisdiction to hear First Pacific's application for entry of judgment; (2) under state contract law, First Pacific could not seek the remedies under the Agreement because it had breached the Agreement by failing to consent to the arbitration; and (3) Petitioners were denied due process. (R-App. IV) Nowhere in any of their submissions did they mention the FAA or make any argument that the trial court had erred by failing to consider federal arbitration law. (*Id.*)

On June 15, 2000,[4] the Court of Appeal affirmed the foreclosure judgment in an unpublished opinion. (P-App. A) It held that even when parties have agreed to arbitrate and to let the arbitrator determine her jurisdiction, a trial court has the right to perform a limited "gatekeeping" function and refuse to send a matter to arbitration when

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[3] First Pacific has attached to this Brief the tables of contents and tables of authorities from Petitioners' various pleadings in the state trial court, Court of Appeal and Supreme Court (and in one instance, the entire pleading because it lacks tables) to demonstrate the procedural failings that First Pacific discusses in the text.

[4] All subsequent dates are in 2000.

the court determines that a party's claim of arbitrability is "wholly groundless." (P-App. A at 5, *citing McCarroll v. L.A. County etc. Carpenters*, 49 Cal. 2d 45 (1957), *abrogated on another point Drake Bakeries v. Bakery Workers*, 370 U.S. 254, 257 (1962)). In this case, the Court held, the parties' agreement to arbitrate disputes arising out of the Agreement did not even arguably contemplate arbitration of the "dispute" relating to Jesus Yujuico's offer to substitute his own renegotiated deal for Petitioners' performance. (P-App. A at 5-6) Accordingly, because Petitioners' claim of arbitrability was wholly groundless, the Court held that the trial court properly declined to refer the matter to arbitration and that the trial court had jurisdiction to enter judgment. (*Id.*)

The Court of Appeal also rejected Petitioners' due process claim. It held that Petitioners had waived their due process rights by agreeing to the stipulated judgment and that in any event, they had received notice and had been given an opportunity to 'fully present their arguments at [the] hearing [on the entry-of-judgment proceeding] and in their motion to vacate the judgment." (*Id.* at 6) Thus, the Court held, Petitioners "received more process than they agreed to accept." (*Id.* at 7)

On June 22, Petitioners filed a petition and request for stay pending further review in the Court of Appeal. (Cal. Ct. App. No. A091568)[5] In that request, Petitioners

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[5] The stay proceedings were the consequence of Petitioners' refusal to post a bond that would have entitled them to a stay of the foreclosure judgment pending appeal. That refusal, combined with Petitioners' refusal to vacate the premises, prompted First Pacific to file an unlawful detainer

claimed, for the first time, that the Court of Appeal's reliance on *McCarroll* conflicted with this Court's decisions. On July 12, the Court of Appeal denied that petition and dissolved a 30-day stay that it had issued before oral argument.

On July 19, Petitioners filed a petition for review (Cal. Supr. Ct. No. S089988), asking the California Supreme Court to stay the unlawful detainer judgment until they had exhausted all appeals from the foreclosure judgment. The next day, Petitioners filed a petition for review of the Court of Appeal's decision in the foreclosure appeal. (Cal. Supr. Ct. No. S090027) In neither of these petitions did Petitioners assert that the trial court's proceedings had denied them due process. (R-App. V-VI) On July 24, the state Supreme Court denied both petitions. Nevertheless, First Pacific could not obtain possession of the premises because the superior court had granted a further (and final) stay of the eviction to September 23.

On September 20 – and with the final stay set to expire – Petitioners served First Pacific with a new complaint they had filed on September 14 in the Northern District of California. (*Yujuico, et al. v. First Pacific Bank Ltd.*, No. C 00-3349 PJH (N.D. Cal.)) In that lawsuit, they

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action in state court. Petitioners removed that action to the Northern District of California, but United States District Judge Saundra Brown Armstrong remanded it to state court. First Pacific then prevailed in the action and obtained a judgment of unlawful detainer. Petitioners then sought seriatim stays throughout the state court system, arguing they "needed time to pack" or other grounds that would not require them to post the bond that they previously had eschewed.

sought to rescind the Agreement on the ground that they had made a mistake of law as to First Pacific's duty to arbitrate sham arbitration demands. They predicated jurisdiction on diversity of citizenship (both First Pacific and Petitioners are foreign residents) and on alleged federal questions arising under the FAA, and sought a temporary restraining order and preliminary injunction that would stay the impending eviction and enjoin a sale of the Atherton property during the pendency of the lawsuit.

On September 22, United States District Judge Phyllis Hamilton heard the matter and denied the request for injunctive relief on the ground that petitioners had "no chance of success on the merits" because (1) their claim could have been brought in the state court litigation, (2) their alleged mistake of law was not reasonable, (3) the court refused to "intermeddle in state court proceedings out of a concern for comity," and (4) Petitioners' lawsuit "may be barred" under *Rooker v. Fidelity Trust Co.*, 263 U.S. 413 (1923), and *Dist. of Columbia Ct. of Appeals v. Feldman*, 460 U.S. 462 (1983). Judge Hamilton also encouraged First Pacific to move to dismiss the lawsuit. Petitioners agreed at the September 22 hearing to voluntarily dismiss, however, and did so on September 27.

On September 28, Petitioners filed a petition for a stay of the foreclosure judgment pending certiorari in the state Court of Appeal. On October 2, the Court of Appeal denied the petition. The following day, Petitioners filed in this Court an application to stay the "mandate" [*sic*] of the California Court of Appeal. Although they had just argued to Judge Hamilton that *they* had mistakenly construed the effect of the arbitration clause, they told this

Court that the *state courts* had mistakenly applied federal arbitration law. (Application For Stay of Mandate, No. 00-A286) Justice O'Connor denied the application on October 3. The eviction went forward as scheduled on that day.

Petitioners now seek certiorari, presenting the same arguments that they made in their stay application to Justice O'Connor.

III

REASONS THE PETITION SHOULD BE DENIED

Petitioners assert as worthy of certiorari one issue they did not raise until after the California Court of Appeal affirmed the foreclosure judgment and a second issue that they failed to present to the California Supreme Court. The first issue is whether state courts have the right, without running afoul of the FAA, to perform a "gatekeeping" function and to decline to refer to an arbitrator wholly groundless arbitrability claims. The second issue is whether the state court's entry of the stipulated judgment after an ex parte proceeding (in which Petitioners participated) and a motion to vacate proceeding (which Petitioners initiated) denied Petitioners due process under the Fourteenth Amendment.

Neither of these issues presents a "compelling" or "important" question – the criteria for review under this Court's rules. S. Ct. R. 10. The unpublished Court of Appeal decision here has no effect on future cases or the development of the law and may not be cited outside the confines of this case. *See* Cal. R. Ct. 977(a). Moreover, both claims that Petitioners raise are not subject to

serious debate, and Petitioners failed to properly press either in the state courts.

A. Petitioners' Failure To Raise In A Timely And Proper Way In The State Courts The Issues They Are Raising In Their Petition Is Reason Alone For The Court To Deny Certiorari

As a matter of comity, this Court will not review a state court judgment unless the party seeking review brought its federal claim "to the attention of the state court with fair precision and in due time." *New York ex rel. Bryant v. Zimmerman*, 278 U.S. 63, 67 (1928). Although one may debate what constitutes "fair precision and in due time," "[a]t the minimum there should be no doubt from the record that a claim under a federal statute or the Federal Constitution was presented in the state courts and that those courts were apprised of the nature or substance of the federal claim at the time and in the manner required by the state law." *Webb v. Webb*, 451 U.S. 493, 501 (1981).

Petitioners failed in several ways to present their present claims "at the time and in the manner required by the state law." *Id.* They did not raise the first claim – an alleged violation of federal arbitration law – in the trial court or in their appeal to the state Court of Appeal until after the Court of Appeal filed its opinion. Each of these failings violated separate state procedural rules. *See Hughes v. Blue Cross of N. Cal.*, 215 Cal. App. 3d 832, 849-53 (1989) (failure to raise claim of federal preemption in state trial court precludes review of preemption issue on appeal); *People v. Scott*, 14 Cal. 4th 544, 553 (1996)

(failure to raise issue in state court of appeal normally bars further review of issue by state supreme court); Cal. R. Ct. 29(b)(1) (same) They also did not raise their second claim – an alleged violation of due process – in the California Supreme Court when they sought review of the Court of Appeal's decision.

As a consequence of Petitioners' failings, no discussion of their first issue appears anywhere in the Court of Appeal opinion that they challenge, and the highest state court was never given an opportunity to rule on their second issue.

Even when this Court *grants* certiorari, it will decline to review issues that the litigants did not fairly present to the state courts. *See Clark v. Jeter*, 486 U.S. 456, 459 (1988) (declining to consider whether federal Child Support Enforcement Amendments preempted state court interpretation of state statute of limitations where litigant failed to adequately present federal question to state courts); *Bankers Life and Casualty Co. v. Crenshaw*, 486 U.S. 71, 77-78 (1988) (declining to consider federal due process claim where petitioner first raised due process issue in petition for rehearing in state supreme court but, even then, did not specify that claim was grounded in federal as well as state constitution); *Webb*, 451 U.S. at 495 (declining to review issue where "nowhere in the opinion of the Georgia Supreme Court is any federal question mentioned, let alone expressly passed upon. Nor is any federal issue mentioned by the dissenting opinion in that court.").

If the failure to properly press a federal issue in the state courts precludes review in those few cases in which

this Court *grants* certiorari, surely petitioners' failure to properly raise their present claims dooms their *request* for certiorari. Indeed, Petitioners do not even attempt to explain these failings – as this Court's rules require – because they cannot. *See* S. Ct. R. 14.1(g)(i) (requiring litigants who seek review of a state court judgment to specify "the stage in the proceedings, both in the court of first instance and in the appellate courts, when the federal questions sought to be reviewed were raised; the method or manner of raising them and the way in which they were passed on by those courts"). The Court should therefore deny the petition for these reasons alone.

B. In Any Event, Neither Of The Issues Petitioners Raise Warrants This Court's Attention

Procedural defects aside, there is no valid reason on the merits for granting certiorari on either of the issues Petitioners have raised. Neither qualifies for certiorari review, and on neither did the state courts err.

1. There Is No Conflict Between The California Supreme Court's *McCarroll* Decision And This Court's Precedents Concerning Arbitral Jurisdiction

This Court consistently has held that the FAA requires a court to apply ordinary contract law to determine whether parties to a contract (1) intended to submit a given dispute to arbitration, and (2) intended that the arbitrator rather than the court would determine the arbitrability of that dispute. *See, e.g., First Options of Chicago v. Kaplan*, 514 U.S. 938, 943 (1995) ("arbitration is simply a

matter of contract between the parties; it is a way to resolve those disputes – but only those disputes – that the parties have agreed to submit to arbitration.").

For almost half a century, the California Supreme Court has adhered to this rule. In *McCarroll v. L.A. County etc. Carpenters*, 49 Cal. 2d 45, the California Supreme Court held: "The arbitrability of a dispute may itself be subject to arbitration if the parties have so provided in their contract. In this situation, the court should stay proceedings pending the arbiter's determination of his own jurisdiction *unless it is clear that the claim of arbitrability is wholly groundless.*" *Id.* at 65 (emph. added).

This holding represents nothing more than an application of the established principle that a court should interpret a contract in a manner that renders it "reasonable and capable of being carried into effect" [Cal. Civ. Code § 1643] and that avoids absurd results [Cal. Civ. Code § 1638]. Thus, if parties to a contract have agreed to let an arbitrator determine her jurisdiction over a dispute, the court must stay proceedings pending the arbitrator's determination of that threshold arbitrability issue. But if the claim of arbitrability is "wholly groundless," the court has the power to intervene to protect the legitimate expectations of the party who never agreed that such a sham claim would be referred to an arbitrator. *See McCarroll*, 49 Cal. 2d at 66 (whether court rather than arbitrator should make the jurisdictional call in the first instance must "reflect the intention of the parties"), 68-69 (principle favoring expansive construction of arbitration provisions "does not justify overriding the parties' intentions and forcing on them a method of decision wholly unexpected in its application").

McCarroll is in accord with federal arbitration law. Under the analogous arbitration provisions of the federal Labor Management Relations Act, one federal court has enunciated the same gatekeeping rule that *McCarroll* articulated. *See Local No. 358 Bakery & Confec., etc. v. Nolde Bros., Inc.*, 530 F. 2d 548, 553 (4th Cir. 1975) ("[T]he arbitrability of a dispute may itself be subject to arbitration if the parties have clearly so provided in the agreement. Of course, the court must decide the threshold question whether the parties have in fact conferred this power on the arbitrator. If they have, the court should stay proceedings pending the arbitrator's determination of his own jurisdiction, *unless it is clear that the claim of arbitrability is wholly groundless.*" (Emph. added); court compelled arbitration under collective bargaining agreement).

Indeed, *McCarroll* itself based its "gatekeeping" rule on federal cases interpreting the FAA. *See McCarroll*, 49 Cal. 2d at 65 (citing *International Un., United Auto. Aircraft v. Benton Harbor Malleable Indus.*, 242 F. 2d 536, 539 (6th Cir. 1957); *Local 205, United Elec. Etc. Workers v. General Elec. Co.*, 233 F. 2d 85, 101 (1st Cir. 1957)). Thus, Petitioners are simply wrong in their claim that federal law "provides no such exception to enforcement of arbitration agreements governed by the FAA." (Petn. at 15)

McCarroll and its federal counterparts are garden variety applications of the FAA rule that, where the parties have agreed to submit contract interpretation questions to the arbitrator, a court's role is "confined to ascertaining whether the party seeking arbitration is making a claim which on its face is governed by the contract." *United Steelworkers v. American Mfg. Co.*, 363

U.S. 564, 568 (1960). Obviously, if it is "clear" that a claim of arbitrability is "wholly groundless," then the party seeking arbitration is *not* making a claim that on its face is governed by the contract.

McCarroll and its federal counterparts also mirror the federal rule that, despite a presumption of arbitrability that might attach to an arbitration agreement, a court should not order arbitration if it can say with "positive assurance" that the parties did not intend the arbitration clause to cover the parties' dispute. *See ITT Hartford Life & Annuity Ins. Co. v. Amerishare Investors, Inc.*, 133 F. 3d 664, 668-70 (8th Cir. 1998) (holding "with positive assurance" that arbitration clause in marketing agreement did not cover action to collect on loan guarantees); *see also Wright v. Universal Maritime Servs. Corp.*, 525 U.S. 70, 78 (1998) (court's "positive assurance" that parties did not intend to arbitrate dispute overcomes presumption of arbitrability that otherwise would attach under the Labor Management Relations Act).

Both the "gate-keeping" rule that *McCarroll* recognized and its identical federal counterpart, together with the rules that courts apply under the FAA, follow logically from the FAA's fundamental command – that the parties' intentions control their obligations to arbitrate and to present an arbitrability claim to an arbitrator in the first instance. *McCarroll* follows that command because, as explained, it seeks strictly to enforce the parties' intentions.

This case demonstrates that a court must retain a limited gatekeeping function to determine if a claim of

arbitrability is "wholly groundless." As the Court of Appeal stated:

> Under [Petitioners'] theory, they could fail to make a payment and file an arbitration demand, alleging that payment was excused because the sky was gray on the payment date. They could then successfully argue that [First Pacific] was in breach by seeking entry of the [stipulated judgment] on the ground that their 'gray sky' 'excuse' for nonpayment gave rise to a dispute that 'arose out of' the [arbitration agreement] and had to be arbitrated, and that only an arbitrator could determine arbitrability. [¶] Once that sham claim of arbitrability was resolved, [Petitioners] could manufacture yet another purportedly arbitrable dispute – claiming for example, that payment was not due because the sun set before 7 p.m. on the payment date. (Opin. at 5-6, *quoting* First Pacific's Respondent's Brief (some brackets in orig.))

Petitioners have never challenged this reasoning. Small wonder, because it is unassailable. Indeed, although the parties here agreed to a broad arbitration clause and to permit an arbitrator to determine arbitrability, they did not reasonably intend to arbitrate everything under the sun or to permit an arbitrator to determine the arbitrability of *any* conceivable dispute. Because courts reject any contract interpretation that produces absurdities – whether or not the contract involves arbitration – the arbitration clause here necessarily permitted a court to exercise a limited gatekeeping power to reject a sham arbitrability demand.

This Court need not grant certiorari to revisit this conclusion because it is self-evident. All courts adhere to

the rule that underlies it, as shown by the unbroken line of decisions by the fourteen jurists who have examined this case.

Because they cannot show any conflict between state and federal law, petitioners instead misstate *McCarroll*'s holding: "The *McCarroll* decision permits judicial consideration of the merits of a dispute governed by the FAA *before* submitting the matter to arbitration if the superior court determines that the claim is 'wholly groundless.' " (Petn. at 3-4, emph. in orig.)

McCarroll does no such thing. When the parties have agreed to permit an arbitrator to determine the arbitrability of disputes arising out of the parties' agreement, *McCarroll* requires a court to submit the claim to arbitration "unless it is *clear* that the *claim of arbitrability* is wholly groundless." 49 Cal. 2d at 65 (emph. added). This is the barest minimum of judicial scrutiny. It permits a court to refuse an arbitrability demand that is a clear sham; it does not permit a court to pass on the merits of the dispute. Indeed, if the court did not retain this minimal gatekeeping power, contracting parties would be powerless to resist a potentially endless series of sham arbitration demands, as the state Court of Appeal here observed. Because Petitioners and First Pacific could not have intended that result, the state courts were correct in relying on *McCarroll* and in refusing to refer this case to arbitration.

To further their invention of a conflict between federal and state law, Petitioners state that *McCarroll* recognized that it was "in 'irreconcilable conflict' with some of the federal decisions at that time. (*McCarroll, supra,* 49

Cal. 2d at 67.)" (Petn. at 5-6) But the "conflict" to which *McCarroll* was referring related to whether a standard collective bargaining agreement requires arbitration – not whether courts may perform a limited gatekeeping role in weeding out sham arbitrability claims. *See* 49 Cal. 2d at 67. As explained, *no* case conflicts with *McCarroll* on the principle at issue here – when parties agree to let an arbitrator determine her jurisdiction over disputes "arising out of the agreement," a court retains a limited gatekeeping function to determine whether an arbitration demand is "wholly groundless."

Having mischaracterized *McCarroll*, Petitioners then draw analogies between it and state laws that this Court has struck down under the FAA. *See Allied-Bruce Terminix Cos. v. Dobson*, 513 U.S. 265, 280-81 (1995) (state statute invalidated all pre-dispute arbitration agreements); *Perry v. Thomas*, 482 U.S. 483, 489-91 (1987) (state statute permitted wage collection action without regard for any private arbitration agreement); *Southland Corp. v. Keating*, 465 U.S. 1, 10-16 (1984) (state statute voided any contract that required franchisee to arbitrate).

But the reason why the statutes at issue in these cases violated the FAA was that they attempted to treat arbitration agreements differently from other contracts, thereby potentially defeating the legitimate expectations of parties to an arbitration agreement. Here, however, *McCarroll*, like the federal cases that are consistent with it, applies ordinary contract law principles to *protect* the parties' legitimate expectations. *McCarroll* thus directs

courts to treat arbitration agreements like any other contract. This is precisely what the FAA requires.[6]

Petitioners also argue that *McCarroll* should be limited to its facts. But nothing in *McCarroll* indicates that its gatekeeping rule should be limited to the context in which *McCarroll* arose. The issue in *McCarroll* was whether contractors who were parties to a collective bargaining agreement ("CBA") with certain labor unions were prohibited from maintaining a lawsuit against the unions for unlawful strikes that the unions had allegedly called, on the ground that the dispute was arbitrable under the CBA. The unions argued that under the CBA, only an arbitrator could determine the arbitrability of the contractors' claim that the unions had violated the CBA's no-strike clause. 49 Cal. 2d at 65-66.

The California Supreme Court held that the trial court properly concluded that the parties did not contemplate arbitration of a breach of the no-strike clause, even though the arbitration clause broadly required arbitration of " 'all grievances or disputes arising between . . . [the parties] over the interpretation or application of the terms of this Agreement. . . . ' " *Id.* at 67. The Court noted that the arbitration clause was contained in "Article V" of the CBA, which was designed to deal with employee complaints concerning "working conditions, wrongful

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[6] *McCarroll* is therefore consistent with the recent Ninth Circuit decision that Petitioners cite. *Portland Gen. Electric Co. v. U.S. Bank Trust Nat. Assoc.*, 218 F. 3d 1085, 1090 (9th Cir. 2000) (because parties' appraisal agreement specified that Oregon law would govern contract, Oregon law, not FAA, governed agreement).

discharge, and the like," and that it was "inconceivable that the parties thought an employer would be required to follow these steps [preliminary complaint to a craft steward, adjudication by a 'special representative,' and eventually arbitration] in prosecuting his objection to a strike." *Id.* at 67-68. Even more persuasive, the Court found, was that the grievance and arbitration procedure was an *alternative* to a strike as the means to settle disputes, "and it is clear that the parties bound themselves to resort to [the grievance] procedure for the very purpose of avoiding the possibility of a strike . . . not to adjudicate a strike once it has occurred. . . . " *Id.* at 68.

What is significant from this discussion is not so much the details and the operation of the particular arbitration provision in *McCarroll*, but that the California Supreme Court found it appropriate to analyze that provision and determine whether the parties' dispute fit within its terms. The Court emphasized that the determination of whether a court rather than an arbitrator should make the jurisdictional call in the first instance was one that needed to "reflect the intention of the parties." *Id.* at 66. And, the Court noted, although courts should construe arbitration provisions in collective bargaining agreements broadly, that principle "does not justify overriding the parties' intentions and forcing on them a method of decision wholly unexpected in its application." *Id.* at 68-69.

This is First Pacific's precise point. Nothing in the Agreement indicates the parties intended to submit a "wholly groundless" "dispute" about a third party's purchase offer to an arbitration between First Pacific and Petitioners, or to permit an arbitrator to determine whether First Pacific's rejection of such a third party offer

would be arbitrable. And nothing in *McCarroll* suggests that its holding concerning judicial responsibility to weed out sham arbitrability demands was limited to the collective bargaining context.[7]

Petitioners correctly note that commercial arbitration agreements that the FAA governs have assumed greater importance in modern life. But that truism provides no basis for reviewing the mundane questions in their petition, on which there is no serious debate in the state and federal courts and which petitioners did not even properly raise below.

2. Even Though They Waived Their Due Process Rights, The Trial Court Gave Petitioners Full Due Process In Connection With Entry Of The Judgment, So There Is No Basis For Their Due Process Claim

Litigants may waive their right to due process by a contract that stipulates to the entry of judgment by expedited process. *See D.H. Overmyer Co. v. Frick Co.*, 405 U.S.

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[7] This Court later abrogated that portion of *McCarroll*'s holding that decided that a standard collective bargaining agreement does not require arbitration. *See Drake Bakeries v. Bakery Workers*, 370 U.S. 254, 257-59 (1962). But nothing in *Drake Bakeries* undermines that portion of *McCarroll*'s holding on which *this* case turns – that when parties agree to let an arbitrator determine her jurisdiction over disputes "arising out of the agreement," a court retains a limited gatekeeping function to determine whether an arbitrability demand is "wholly groundless." Thus, as the state Court of Appeal recognized, *Drake Bakeries* does not affect the application of the relevant *McCarroll* principle here. (P-App. A at 6 n.3) Petitioners' suggestion to the contrary is wrong. (*See* Petn. at 6)

174, 187 (1972) (debtor waived right to notice and hearing before deprivation of property when, while represented by counsel, debtor signed a document that authorized judgment by confession); *FRG, Inc. v. Manley*, 919 F. 2d 850, 857 (3d Cir. 1990) (party waived due process rights where "the confession of judgment clause here was negotiated and specifically agreed upon in a commercial context in settlement of major litigation between parties represented by counsel").

Consistent with these principles, California law authorizes such due process waivers in order to permit the prompt and efficient resolution of litigation. *See Rooney v. Inv. Co.*, 10 Cal. 3d 351, 358 (1973) ("When a written stipulation sets forth all the terms of a judgment agreed to by the parties, the filing of the stipulation normally provides sufficient basis for entry of judgment upon the ex parte application of either party."). This common sense rule easily satisfies the Fourteenth Amendment because it simply enforces a litigant's bargained for stipulation to expedited process.

Here, while represented by counsel and after lengthy negotiations, Petitioners agreed that if they breached the Agreement, First Pacific could obtain entry of the Judgment "without further notice" to Petitioners. (P-App. A at 2, 6) That waiver was part of the consideration for First Pacific's agreement to shave millions of dollars off of Petitioners' debt and to give them yet another chance to make good on their loan obligations. Because Petitioners voluntarily and intelligently waived their due process rights for valuable consideration, the state trial court constitutionally could have entered judgment without

affording petitioners notice and an opportunity to be heard.

But the state trial court *did* afford petitioners that notice and opportunity. They received notice of the setting of the ex parte hearing on the entry of judgment and appeared on the day the hearing was set. They also presented written opposition to the trial judge and conveyed oral argument through the judge's research attorney. (P-App. A at 4, 6) And, although no more was required, they then filed and set a hearing on a motion to vacate the judgment. The hearing would have occurred but for *Petitioners'* decision not to contest the court's tentative ruling, which was against them. (*Id.*; R-App. I) Each of these procedures gave Petitioners ample opportunity to raise any arguments in opposition to entry of the judgment of foreclosure. *See In re Marriage of Jacobs*, 128 Cal. App. 3d 273, 285-86 (1982) (under California law stipulated judgment will be set aside if moving party demonstrates grounds for vacating the judgment). Considering that Petitioners expressly waived their due process rights, the notice and opportunity to be heard that they received easily satisfied the Fourteenth Amendment.

Petitioners have not cited a single case that found a due process violation on even remotely analogous facts, much less demonstrated a substantial conflict or confusion in the lower courts on this issue. Their due process claim is so flimsy that even they omitted it from their petition for review in the California Supreme Court. This Court need not grant certiorari to review a claim that even the petitioners did not think worthy of a state high court's review.

IV

CONCLUSION

Petitioners are raising claims here that they did not properly present to the state courts below. Their current claims neither address nor involve any substantial questions of law, and the state Court of Appeal's decision has no precedential value. The parties and the system already have invested far more resources examining this matter than this case merits. This Court should therefore deny the petition for a writ of certiorari.

Dated: November 9, 2000.

Respectfully submitted,

PAUL D. FOGEL
Counsel of Record
ANTHONY THEOPHILOS
MICHAEL E. DELEHUNT
RAYMOND A. CARDOZO

CROSBY, HEAFEY, ROACH & MAY
PROFESSIONAL CORPORATION

Attorneys for Respondent
First Pacific Bank Limited

APPENDIX I

Michael E. Delehunt (CSBN 070619)
Philip L. Tudor (CSBN 148065)
CROSBY, HEAFEY, ROACH & MAY
Professional Corporation
4 Embarcadero Center
Suite 1900
San Francisco CA 94111
Telephone: (415) 543-8700
Facsimile: (415) 391-8269

First Pacific Bank Limited,
a Hong Kong banking corporation

SUPERIOR COURT OF CALIFORNIA –
COUNTY OF SAN MATEO

FIRST PACIFIC BANK LIMITED, a Hong Kong banking corporation,

Plaintiff,

vs.

THE BVY GROUP, a California Corporation, et al.,

Defendants.

_____/

THE BVY GROUP, a California corporation, et al.,

Cross-Complainants,

vs.

FIRST PACIFIC BANK LIMITED, a Hong Kong banking corporation, et al.,

Cross-Defendants.

_____/

No. 391951

ORDER DENYING DEFENDANTS' THE BVY GROUP, INC., BENEDICTO V. YUJUICO AND TERESITA YUJUICO'S MOTION TO VACATE JUDGMENT

Date:
December 3, 1998
Time: 9:00 a.m.
Dept.:
Law & Motion;
Dept. 10

(Filed Dec. 8, 1998)

Defendants' motion to vacate judgment was set for hearing in Department 10 of the above-entitled court before the Honorable Judith Whitmer Kozloski, on December 3, 1998. The Court, having considered the pleadings and all documents filed relating to defendants' motion, and good cause appearing, issued its tentative ruling on December 2, 1998 pursuant to San Mateo County Superior Court Local Rule 3.5, denying defendants' motion to vacate the judgment. There having been no appearance by counsel for the parties to contest the tentative ruling, IT IS HEREBY ORDERED that:

Defendants' motion to vacate judgment is denied.

DATED: December 8, 1998

By Judith Whitmer Kozloski
Honorable Judith Whitmer Kozloski
Judge of the Superior Court

APPENDIX II

MICHAEL J. COFFINO (SBN 88109)
ELIZABETH H. MURPHY (SBN 174095)
TATRO COFFINO ZEAVIN BLOOMGARDEN LLP
116 New Montgomery Street, Suite 640
San Francisco, California 94105
Telephone: (415) 427-1015
Facsimile: (415) 427-1017

Attorneys for Defendants and
Cross-Complainants BVY, the BVY Group,
Benedicto V. Yujuico and Teresa Yujuico

**SUPERIOR COURT OF THE STATE OF CALIFORNIA
IN AND FOR THE COUNTY OF SAN MATEO**

FIRST PACIFIC BANK LIMITED, a Hong King banking corporation, First Pacific, v. THE BVY GROUP, a California corporation; et al., Defendants.	Case No. 391951 **MEMORANDUM OF POINTS AND AUTHORITIES IN OPPOSITION TO EX PARTE APPLICATION FOR ENFORCEMENT OF ARBITRATION AWARD AND ENTRY OF STIPULATED JUDGMENT**
AND RELATED CROSS-ACTIONS.	Date: October 9, 1998 TIME: 2:00 p.m. DEPT: 10

Defendants and Cross-Complainants the BVY Group, Benedicto V. Yujuico and Teresita Yujuico (collectively, "BVY") hereby respectfully submit the following Memorandum of Points and Authorities in Opposition to the

Ex Parte Application of First Pacific First Pacific Bank ("First Pacific") for Enforcement of Arbitration Award and Entry of Stipulated Judgment (the "Application"):

INTRODUCTION

This court lacks jurisdiction to hear First Pacific's Application. As we show, the parties are subject to a broad and all encompassing arbitration agreement pursuant to which they agreed to submit to binding arbitration "any dispute" between them "relating to or arising out of" a settlement agreement reached in this action in August 1997. On October 2, 1998, BVY submitted to JAMS/Endispute ("JAMS"), the tribunal selected to preside over any dispute under the settlement agreement, a Demand for Arbitration seeking resolution of pending disputes concerning performance under the settlement. Thus, on that date, arbitration proceedings commenced and this Court does not, respectfully, have jurisdiction to hear this matter.

By its Application, First Pacific seeks the entry of a judgment that exceeds by $2,300,000 the agreed-upon settlement amount, following First Pacific's unreasonable and improper rejection of a timely tender of performance under the settlement agreement. As we show, this tender would have made First Pacific whole and was entirely reasonable. Thus, bona fide disputes exist as to whether BVY is in default and whether First Pacific is entitled to seek entry of judgment. These issues, together with the jurisdictional question, if any, must be decided in arbitration.

Even if the Court were to reach the substantive issues that now exist, which it should not, it must nonetheless decline to grant the requested relief. First, First Pacific is not entitled to entry of judgment because there has been no breach. BVY has already paid 65% of the amount owing and has tendered to First Pacific the balance on terms that actually *improve* the position of First Pacific. This tender constitutes substantial performance under applicable law and prevents a finding of default. What is more, even if this Court had jurisdiction and even if BVY had breached the Agreement, the difference between the $5,200,000.00 agreed-to and the $7,500,000.00 value of the proposed judgment constitutes an unenforceable forfeiture and a penalty. The circumstances giving rise to the present dispute provide a compelling case for application of the equitable and statutory principles that preclude forfeiture of real property and the imposition of penalties.

First Pacific's Application is nothing more than an improper attempt to circumvent the clear terms of the arbitration agreement and to obtain an improper forfeiture. Accordingly, BVY respectfully submits that this Application must be summarily denied.

II. STATEMENT OF FACTS

A. The Underlying Settlement And Arbitration Agreements

On or about August 1, 1997, BVY Group, Benedicto V. Yujuico and Teresita Yujuico (collectively, "BVY") and First Pacific entered into an Agreement of Compromise and Settlement, Release, and Covenant Not To Sue (the

"Agreement"), in settlement of this litigation. Pursuant to the Agreement, BVY agreed to pay First Pacific the total sum of $5.2 million in three installments of $3 million, $1.1 million and $1.1 million on August 29, 1997, January 15, 1998 and August 15, 1998, respectively. A residence belonging to defendants and cross-complainants Benedicto and Teresita Yujuico in Atherton, California, secured these payment obligations ("the Property"). Declaration of Benedicto V. Yujuico ("Yujuico Decl.") ¶ 3.[1] The Agreement further provides that if BVY commits a payment default, First Pacific may submit a request to the Court to enter a Stipulation for Enforcement of Arbitration Award and Stipulated Judgment in the increased amount of $7,500,000.00 and may seek to foreclose nonjudicially on the Property. Yujuico Decl., Exh. A.

In negotiating the Agreement, First Pacific insisted that any disputes that might arise in connection with the Agreement be submitted to arbitration. Coffino Decl. ¶ 3. First Pacific also insisted that the arbitration be controlled by the International Arbitration Rules of the American Arbitration Association. Coffino Decl. ¶ 3. Accordingly, First Pacific, who drafted the settlement documentation, included in the Agreement an exclusive and all-encompassing arbitration clause. Coffino Decl. ¶ 3. Specifically, the Agreement provides as follows: **"In the event of any dispute relating to or arising out of [the] Agreement, the**

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[1] The Yujuico Declaration is attached to the Declaration of Michael J. Coffino ("Coffino Decl.") as Exhibit 1 and is in facsimile form. Because First Pacific has elected to proceed on an ex parte basis and Mr. Yujuico is in the Philippines, we had no choice but to obtain a facsimile declaration.

exclusive forum for resolution of any such dispute shall be by arbitration in San Francisco, California under the authority of JAMS/Endispute in accordance with the International Arbitration rules of the American Arbitration Association (the "Arbitration Rules"). Yujuico Decl., Exh. A ¶ 19.

B. Performance by BVY Under the Agreement

In accordance with the Agreement, BVY timely made the initial $3 million payment to First Pacific. Subsequently, the entire Asian continent became plagued by one of worst economic crises in our time. In the third quarter of 1997, for example, the exchange rate for the Philippine peso was P26 to US$1.00; today, the rate is approximately P44 to US$1.00. Yujuico Decl. ¶ 2. In January 1998, in light of difficult economic circumstances, BVY negotiated a restructuring with First Pacific in the form of an amendment to the Agreement ("the Amendment"). Under the Amendment, First Pacific increased the interest rate to 9.5% (from 7%) and altered the payment schedule. The Amendment states that several payments totaling $450,000 would be paid over the course of several months in different amounts. The next $450,000 would be due on September 15, 1998; the next $650,000 on March 15, 1999; and the final $650,000 on September 15, 1999. Yujuico Decl., Exh. B.

Despite very difficult economic circumstances, BVY made the six payments called for between February and August 1998 pursuant to the Amendment. BVY would always advise First Pacific in advance of any difficulty anticipated in meeting a strict due date and invariably

First Pacific would consent to an extension of the due date. As detailed in prior declarations in the underlying litigation that culminated in the Agreement, First Pacific and BVY have had a very unique relationship, which has included, among other things, stock ownership by First Pacific Bank in BVY and a long history of restructures and oral and informal agreements. Yujuico Decl. ¶ 7. To date, BVY has paid $3,450,000 and has tendered the $450,000 due on September 15, 1998, which, as explained below, First Pacific declined to accept.

On September 9, 1998, due to a variety of economic circumstances, the father of Benedicto Yujuico, Jesus Yujuico, offered to *improve* the payment schedule set forth in the Amendment. He offered to pay First Pacific $450,000 on September 16, 1998 and the entire balance of $1,300,000 on March 15, 1999, even though the final $650,000 was not due until September 15, 1999. In connection with this tender, Mr. Jesus Yujuico requested that First Pacific sell him the BVY note and take a new note on the terms outlined above. He agreed that First Pacific would retain all the same collateral (including the Arbitration Award and Stipulated Judgment). He also offered to pay all of First Pacific's legal fees and $10,000 of its administrative costs in preparing necessary documentation. Yujuico Decl. ¶ 9. First Pacific rejected this tender of performance. By letter dated September 30, 1998, First Pacific demanded payment of the $450,000 due on September 15, 1998. Yujuico Decl., Exh. C. Despite the rejection of the tender, BVY remains willing to perform in accordance with the tender of performance. As a good faith gesture, BVY is also willing to put in escrow 50% of

what is due currently under the Amendment pending the outcome of the arbitration proceedings.

C. Commencement of Arbitration

On October 2, 1998, BVY served on First Pacific and its counsel and submitted by hand delivery to JAMS, the arbitration tribunal selected by First Pacific, a Demand for Arbitration in accordance with Paragraph 19 of the Agreement. Coffino Decl. ¶ 4 & Exh. 2 (Demand). Pursuant to Article 2 of the Arbitration Rules, the submission the arbitration demand commenced arbitral proceedings. Coffino Decl., Exh. 3 (Rules). "Arbitral proceedings shall be deemed to commence on the date on which the administrator receives the notice of arbitration." *Id.*

On October 5, 1998, at the request of BVY, JAMS scheduled a hearing for October 15, 1998 to determine whether First Pacific was required to participate in the arbitration and to determine whether First Pacific should be restrained – pursuant to Article 21 of the Arbitration Rules allowing injunctive relief – from seeking Court intervention pending the outcome of the arbitration. Coffino Dec. ¶ 5. On October 7, 1998, First Pacific confirmed its willingness to appear at the hearing subject to a reservation of rights. Coffino Decl., Exh. 3. The very next day, however, First Pacific attempted to make an end-run around the arbitration agreement by notifying BVY of this Ex Parte Application.

III. LEGAL ARGUMENT

A. This Court Lacks Jurisdiction To Hear First Pacific's Application

Upon the commencement of arbitration proceedings, the arbitrator "takes over" and in consequence assumes exclusive jurisdiction to decide all questions needed to resolve the controversy and all issues relating to procedure and discovery. *Van Tassel v. Superior Court*, 12 Cal. 3d 624, 627 (1974); *Titan/Value Equities Group, Inc. v. The Superior Court of San Diego County*, 29 Cal.App. 4th 482, 487-88 (1994); Accordingly, once a case is submitted to arbitration, the trial court lacks jurisdiction to resolve procedural questions, order discovery or determine the status of claims before the arbitrator. *Id.* at 489.

Here, BVY commenced arbitration on October 2, 1998 in accordance with the rules selected by First Pacific. By so doing, BVY properly invoked the jurisdiction of the arbitration tribunal, also selected by First Pacific, to determine whether in fact BVY committed a default under the terms of the Agreement. This central issue is unequivocally a "dispute relating to or arising out of [the Agreement]," which falls squarely within the parties' arbitration agreement. In addition, JAMS must decide the nature of the rights and obligations under the Agreement under the present circumstances whether and, if so, to what extent, First Pacific Bank may enforce the Agreement at this time.

We anticipate that First Pacific will argue there is no arbitrable dispute worthy of arbitration. Such an argument betrays a misunderstanding of the arbitrable process and the jurisdiction of the arbitrator. It is well settled

that it is the province of the arbitrator, not that of the Court, to decide questions of his or her jurisdiction. C.C.P. §§ 1297.161-163; *McCarroll v. L.A. County Carpenters* (1957) 49 Cal.2d 45, 65-66. Not surprisingly, the Arbitration Rules expressly vest the arbitrator with the authority to decide issues of jurisdiction. Article is Exhibit "1" hereto. Indeed, in international arbitrations, challenges to the jurisdiction of the arbitrator are made *in the arbitration*. C.C.P. § 1297.162. Court involvement is expressly limited to reviewing jurisdictional decisions made *by the arbitrator* during the course of those proceedings. C.C.P. § 1297.166.

The attempt by First Pacific to embroil the Court in this process, is a breach of the arbitration clause and, if permitted, would eviscerate a provision in the Agreement that First Pacific demanded be made a material part of the compromise reached last year. Equally important, the attempt by First Pacific to ignore the arbitration clause is squarely at odds with the Arbitration Rules it insisted must govern future disputes between the parties, contravenes the provisions of code of Civil Procedure governing international arbitration and offends the spirit and sanctity of the arbitration process.

For these reasons, the Court must, we respectfully submit, deny the ex parte application submitted by First Pacific.

B. There Are Bona Fide Disputes Subject to Arbitration

Although we believe that this court may not decide the jurisdiction of the arbitrator at this time, and thus

submit that whether or not an arbitrable dispute exists is entirely irrelevant to the Application, we now show that a bona fide dispute exists under the Agreement that must be resolved by arbitration before First Pacific may, if at all, proceed to invoke the jurisdiction of this Court.

1. BVY Have Substantially Performed Under The Agreement

Under the doctrine of substantial performance, a party who has "substantially performed" the terms of a contract may be entitled to complete performance under the agreement, rather than be subject to damages for default. Corbin, *Contracts*, §§ 700-701 (West Publishing 1982). In general, a party has substantially performed if there has been no willful departure from the terms of the contract, the party has in good faith performed all of the substantive terms of the contract, and the "defect" can be easily remedied such that the other party will get "almost" what the contract requires. *Posner v. Grunwald-Marx, Inc.*, 56 Cal. 2d 169, 187 (1961); *Bonadelle Constr. Co. v. Hernandez*, 169 Cal. App. 2d 396, 399 (1959); Corbin § 707 (the higher the ration of performance to non-performance, the more likely there has been substantial performance); *Scarbery v. Patch Land and Water Co.*, 184 Cal.App. 2d 87, 105 (1960) (payment of $150,000 of a $200,000 obligation found substantial enough to outweigh default).[2]

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[2] The doctrine is consistent with the concept of a "material breach," which is determined pursuant to the following factors: (i) the extent to which the injured party will obtain the

In determining whether a party has substantially performed, a party's good faith or, alternatively, willfulness in performing must be taken into account. *Id.* Thus, in *Commercial Discount Co. v. Town of Plainfield* 180 A. 311 (1935), a contractor who had completed approximately 90% of a construction job but who was forced to cease work due to financial difficulties was considered not to have behaved willfully or intentionally and, thus, to have substantially performed the contract.

It is plain that under applicable law whether a party has substantially performed presents a fact question for the trier of a fact. Here, there is no question that BVY have substantially performed the Agreement. Each of the payments due prior to September 15, 1998 was made in full and accepted without complaint. To date, BVY have paid a total of $3,450,000 of principal under the Agreement, which represents approximately 65% of the total principal obligation. Moreover, BVY tendered performance of the balance of the payment obligations on terms that provided First Pacific with a *better* economic package than what is in place. It only asked for an immaterial alteration of the documents which did not prejudice First

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substantial benefit of what he expected; (ii) the extent to which the injured party may be adequately compensated in damages for lack of complete performance; (iii) the extent to which the party failing to perform has already partly performed; (iv) the degree of hardship the defaulting party would suffer on termination of the contract; (v) the willfulness or innocence of the non-performing party; and (vi) the degree of certainty that the party will complete performance. *Sackett v. Spindler* (1967) 248 Cal.App.2d 220, 229.

Pacific in any way. In fact, it even offered to pay for the costs of making those minor alterations.

This performance comes in the middle of a severe repression that is undermining markets in Asia in an unprecedented and alarming manner. The circumstances surrounding the creation of the Agreement have changed dramatically. Still, BVY has at all times acted reasonably and have attempted to live up to the strict terms of the Agreement. It has acted in utmost good faith and, as a further gesture of good faith, has even offered to put a substantial sum in escrow pending the outcome of the arbitration. Yujuico Decl. ¶ 13.

The slight document alteration requested by BVY is fully consistent with the course of dealing that has existed between the parties. Over the course of several years, as shown in the underlying litigation, the parties constantly revised and restructured their relationship, often orally without documentation. Yujuico Decl. ¶ 7. Indeed, when the economic crisis hit the Philippines, the parties did yet another restructure that resulted in the Amendment. Paragraph 20 of the Agreement, pursuant to which First Pacific agreed "to execute all instruments and take all such actions are reasonably requested and appropriate to effectuate this Agreement."[3]

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[3] It is well settled that a lender's acceptance of performance that deviates from the strict contact terms and overall cooperation and informality lulls borrowers into a sense of security, which cannot then be snatched away at a moments' notice. In *Lupertino v. Carbahal* 35 Cal. App. 3d 742 (1973), after undertaking a course of conduct that instilled in the borrowers a sense of comfort and reliance, the lender was thereafter

What is more, an arbitrator has the power and authority to require that First Pacific accept the tender of performance made this September. As recognized by the California Supreme Court in *Advanced Micro Devices v. Intel Corp.* (1994) 9 Cal. 4th 362, 374, this case, it "may require finding a way of approximating the impact of a breach that cannot with any certainty be reduced to monetary terms. **Passage of time and changed circumstances may have rendered any remedies suggested by the contract insufficient or excessive.**" *Id.* Indeed, the arbitrator in this case will be required to "bring his informed judgment to bear to reach a fair solution." *Steelworkers v. Enterprise Corp.* (1960) 363 U.S. 593, 597; 4 L.Ed.2d 1424, 1428; 80 S.Ct. 1358 (recognizing the need for flexibility in meeting a wide variety of situations, where draftsmen may never have thought of particular contingency).

The arbitrator's ability to fashion creatively an appropriate remedy based upon the parties' varying interpretations of the Agreement is consistent with the exceedingly broad powers that arbitrators generally enjoy and frequently implement. In *Moncharsh v. Heily Blasé* 3 Cal. 4th 1, 28 (1992); for example, the arbitrator resolved

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estopped from summarily abandoning such conduct without, at the very least, providing notice sufficient to allow the borrower to complete performance. Similarly, in *Lopez v. Bell* (1962) 207 Cal.App.2d 394, 399, the lender established a pattern of accepting late payments, thereby "lulling" the borrower into a sense of security. Ultimately, the court set aside the trustee's sale, holding that absent a specific notice reinstating the lender's intention to seek strict compliance with the terms of the contract, the lender's conduct amounted to a waiver of strict compliance and the right to forfeit the borrowers' interest. Id. at 397-98.

issues that the parties had not even agreed to arbitrate. Recognizing that resolution of "all contested issues" is exactly what the parties bargained for in the arbitration agreement, the court found that the arbitrator had not exceeded his authority and confirmed the award. *Id.* Similarly, in *Morris v. Zuckerman* 69 Cal. 2d 686, 688-94 (1968), the court confirmed an award which created a condition to the required sale, even though the original contract had no such limitation. *See also Anderman/Smith Co. v. Tenn Gas Pipeline Co.*, 98 F.2d 1215, 1217-20 (court approved award altering contract provisions for price changes in natural gas pricing).

2. The Stipulated Judgment And Arbitration Award are Unenforceable Forfeitures

An important principle that will guide the disposition of the arbitration is that "the law abhors a forfeiture." This principle is codified in Cal. Civil Code § 3275, which provides that "whenever, by the terms of an obligation, a party thereto incurs a forfeiture, or a loss in the nature of a forfeiture, by reason of his failure to comply with its provisions, he may be relieved therefrom, upon making full compensation to the other party, except in case of a grossly negligent, willful or fraudulent breach of duty." *Id. See also Nasir v. Sacramento County Office of the District Attorney* 11 Cal. App. 4th 976, 993-94 (1992).

The Agreement in this case contains two separate but equally abhorrent forfeitures. Indeed, Section 3275 has been interpreted to prohibit both the forfeiture of real property, where the borrower has in good faith attempted to avoid a default, and the forfeiture of money that

results from the enforcement of "hammer clauses" such as the $7.5 million stipulated Arbitration Award in this case. *Barkis v. Scott*, 34 Cal.2d. 116; *Scarbery v. Patch*, 184 Cal.App.2d 87 (1960); *Chambreau v. Coughlan*, 263 Cal.App.2d 712 (1968); *L.A. City Sch. Dist. v. Landier, Inc.*, 177 Cal.App.2d 744 (1960).

As to the first type of forfeiture, *Scarbery* is instructive. In *Scarbery*, the parties entered into a complicated lease option agreement, pursuant to which the plaintiff was to make payments for a specified period and that, upon an uncured default thereunder, the defendant would retain all amounts paid as liquidated damages and become the owner in fee of the property. For two years, the plaintiff made all payments and significantly improved the property. However, because of an intervening fire in the area and the plaintiff's unrelated physical illness, the property did not generate sufficient income for the plaintiff to meet his obligations under the lease option. Although the plaintiff subsequently tendered performance sufficient to reinstate the contract, the defendant refused and attempted to foreclose on the property.

In balancing the equities, the court found that because the plaintiff had paid $150,000 of a $200,000 obligation, his part performance was substantial enough to outweigh the degree of default, particularly since the court could easily measure the damage suffered by the default. The court also weighed heavily the fact that the plaintiff's nonpayment was due to inability rather than

unwillingness.[4] Accordingly, the Court ordered, pursuant to Section 3275, relief from the forfeiture.

Here, Claimants, like the defendant in *Scarbery*, face possible forfeiture of real property notwithstanding their good faith efforts to perform and the unforeseeable events in Asia. Further, Claimants have demonstrated an ongoing willingness to perform in full by, among other things, offering to repay the remaining sums on **better** terms than original terms and offering to place disputed amounts in escrow pending resolution of these issues. Under *Scarbery*, therefore, BVY is entitled to relief from the real property forfeiture now threatened by Plaintiff.

Section 3275 also applies in this instance to prevent enforcement of First Pacific's $2,300,000 "hammer clause." In *Chambreau, supra*, the parties stipulated to judgment for $8,025, but agreed to stay execution provided defendant paid for the lesser sum of $5,500.00 in regular monthly installments. Like First Pacific, the *Chambreau* plaintiff attempted to execute on the greater judgment based upon one late payment. The court properly disallowed the plaintiff's attempt to execute on the greater judgment, concluding that the defendant was entitled to equitable relief from forfeiture under Section 3275. Similarly, in *L.A. City Sch., supra*, the parties stipulated that the defendant would pay a sum certain in 8 annual installments, but that, following an uncured 30 day default, judgment could be entered for twice the unpaid balance. Although the defendant's request for

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[4] See also, *Ebbert v. Merchantile Trust Co. of Cal.* 213 Cal. 496, 500 (1931).

declaratory relief was found untimely, the court noted that the economic sanction constituted an improper penalty. *Id.* at 754.

Accordingly, First Pacific's proposed Judgment is unenforceable both as a real property forfeiture and a monetary penalty.

IV. CONCLUSION

Based upon the foregoing, BVY respectfully submits that the Application must be denied.

Dated: October 9, 1998

Respectfully submitted,

TATRO COFFINO ZEAVIN
BLOOMGARDEN

By: /s/ E Murphy
Elizabeth H. Murphy
Attorneys for Defendants,
Cross-Complainants
and BVY The BVY Group,
Benedicto V. Yujuico and
Teresa Yujuico

APPENDIX III

MICHAEL J. COFFINO (SBN 88109)
ELIZABETH H. MURPHY (SBN 174095)
TATRO COFFINO ZEAVIN BLOOMGARDEN LLP
116 New Montgomery Street, Suite 640
San Francisco, California 94105
Telephone: (415) 427-1015
Facsimile: (415) 427-1017

Attorneys for Defendants and
Cross-Complainants The BVY Group,
Benedicto V. Yujuico and Teresita Yujuico

SUPERIOR COURT FOR THE STATE OF CALIFORNIA
IN AND FOR THE COUNTY OF SAN MATEO

FIRST PACIFIC BANK LIMITED, a Honk Kong banking corporation, Plaintiff, vs. THE BVY GROUP, a California corporation; et al., Defendants. AND RELATED CROSS-ACTIONS	Case No. 391951 **MEMORANDUM OF POINTS AND AUTHORITIES IN SUPPORT OF MOTION TO VACATE JUDGMENT** **[C.C.P. § 473]** **Date: December 3, 1998** **Time: 9:00 a.m.** **Dept: Law & Motion** **(Filed Nov. 18, 1998)**

Table Of Contents

		Page
I.	INTRODUCTION	1
II.	STATEMENT OF FACTS	2
	A. The Underlying Settlement Agreement And Arbitration Clause	2
	B. Performance By BVY Under The Agreement	3
	C. Commencement Of Arbitration	4
	D. Entry Of The Judgment	4
III.	LEGAL ARGUMENT	5
	A. For Two Independent Reasons, – Lack Of Jurisdiction And Violation Of Due Process – The Judgment Is Void	5
	1. The Court Did Not Have Jurisdiction To Enter The Judgment	6
	2. Even Assuming The Court Had Jurisdiction To Enter The Judgment Without An Evidentiary Trial Violated Due Process	11
IV.	CONCLUSION	13

Table of Authorities

Cases	Page
Abelleira v. District Court of Appeal, 17 Cal. 2d 280 (1941)	5
Baker v. Aubry, 216 Cal. App. 3d 1259 (1989)	9

Byerly v. Sale, 204 Cal. App. 3d 1312 (1988) 6, 7

Bonadelle Constr. Co. v. Hernandez, 169 Cal. App. 2d 396 (1959) 8

Chambreau v. Coughlan, 263 Cal. App. 2d 712 (1968) 8

County of Los Angeles v. Soto, 35 Cal. 3d 483 (1984) 11

County of Ventura v. Tillett, 133 Cal. App. 3d 105 (1982) 11

Ericksen v. 100 Oak Street, 35 Cal. 3d 312 (1983) 7

Estate of Buchman, 123 Cal. App. 2d 546 (1954) 11

Federal Insurance Company v. Superior Court, 60 Cal. App. 4th 1370 (1998) 8

Felner v. Metropolitan Ins. Co., 6 Cal. App. 3d 540 (1970) 6, 9

Isbell v. County of Sonoma, 21 Cal. 3d 61 (1978) 11

Izzy v. Mesquite Country Club, et al., 186 Cal. App. 3d 1309 (1986)..... 4

Jones v. World Life Research Institute, 60 Cal. App. 3d 836 (1976)..... 5

L.A. City Sch. Dist. v. Landier, Inc., 177 Cal. App. 2d 744 (1960) 8

Lopez v. Bell, 207 Cal. App. 2d 394 (1962) 8

Lupertino v. Carbahal, 35 Cal. App. 3d 742 (1973) 8

McCarroll v. Los Angeles County District Council of Carpenters, 49 Cal. 2d 45 (1957)..... 10

Orpustan v. State Farm Mut. Auto. Ins Co., 7 Cal. 3d 988 (1972)..... 6

Posner v. Grunwald-Marx. Inc., 56 Cal. 2d 169 (1961) 8

Rooney v. Vermont Investment Corp., 10 Cal. 3d 351 (1973) 5, 6, 11, 12, 13

Scarbery v. Patch, 184 Cal. App. 2d 87 (1960) 8

Titan/Value Equities Group, Inc. v. The Superior Court of San Diego County, 29 Cal. App. 4th 482 (1994) 6, 7

Van Tassel v. Superior Court, 12 Cal. 3d 624 (1974) 6

Statutes and Rules

California Code of Civil Procedure

§ 473 5

§ 1297.161 10

§ 1297.162-166 10

California Civil Code

§ 3275 8

California Evidence Code

§ 452(g) 4

§ 459(a) 4

* * *

APPENDIX IV

Case No. AO85195

IN THE COURT OF APPEAL OF THE
STATE OF CALIFORNIA

FIRST APPELLATE DISTRICT

DIVISION FOUR

FIRST PACIFIC BANK LIMITED, a Hong Kong Banking Corporation,	)
Plaintiff and Respondent,	)
v.	)
BENEDICTO YUJUICO, TERESITA YUJUICO, and THE BVY GROUP, INC.,	)
Defendants and Appellants.	)

Appeal from the Superior Court of San Mateo County
Case No. 391951
Honorable Judith Whitmer Kozloski, Judge

APPELLANTS' OPENING BRIEF

Gerald M. Murphy, Esq.
[State Bar No. 99994]
Michele A. Firpo, Esq.
[State Bar No. 140012]
JACOBS, SPOTSWOOD, CASPER
& MURPHY, LLP
One Maritime Plaza, Suite 400
San Francisco, California 94111

Telephone No.: (415) 835-3700
Facsimile No.: (415) 835-1072

Attorneys for Defendants
and Appellants
BENEDICTO YUJUICO, TERESITA
YUJUICO and THE BVY GROUP, INC.

TABLE OF CONTENTS

	Page
TABLE OF AUTHORITIES	i
I. SUMMARY OF ARGUMENT	1
II. STATEMENT OF FACTS	3
A. The Settlement Agreement and Mandatory Arbitration Provision	3
B. The Asian Economic Crisis and Amendment to the Agreement	5
C. Appellants' Demand For Arbitration	7
D. Respondent's Void Ex Parte Judgment	8
III. STATEMENT OF APPEALABILITY	9
IV. LEGAL DISCUSSION	9
A. THIS APPEAL PRESENTS A QUESTION OF LAW SUBJECT TO THIS COURT'S INDEPENDENT REVIEW	9
B. RESPONDENT DID NOT HAVE STANDING TO SEEK ENTRY OF THE EX PARTE JUDGMENT AND PENALTY DAMAGES	11

1. Respondent Unlawfully Ignored Appellants' Demand for Arbitration Pursuant to the Terms of the Settlement Agreement 12

C. RESPONDENT CANNOT ENJOY THE BENEFITS OF CONTRACTUAL REMEDIES CREATED BY ITS OWN BREACH 15

D. APPELLANTS WERE DENIED DUE PROCESS OF LAW BY THE EX PARTE ENTRY OF THE JUDGMENT OF FORECLOSURE 17

V. CONCLUSION 20

TABLE OF AUTHORITIES

Page

Cases

Abelleira v. District Court of Appeal (1941) 17 Cal.2d 280 [109 P.2d 942] 12, 13

Antonelle v. Kennedy & Shaw (1903) 140 Cal. 309 [73 P. 966] 15

Brookwood v. Bank of America (1996) 45 Cal.App.4th 1667 [53 Cal.Rptr.2d 515] 10

City of Manhattan Beach v. Superior Court (1996) 13 Cal.4th 232 [52 Cal.Rptr.2d 82, 914 P.2d 160] 9, 10

Clothesrigger, Inc. v. GTE Corp. (1987) 191 Cal.App.3d 611 [236 Cal.Rptr. 605] 9

County of Venture v. Tiller (1982) 133 Cal.App.3d 105 [183 Cal.Rptr. 741] 17

Davies Machinery Co. v. Pine Mountain Club, Inc. (1974) 39 Cal.App.3d 23 [113 Cal.Rptr. 784] 9

Erickson, Arbuthnot, McCarthy Kearney & Walsh, Inc. v. 100 Oak Street (1983) 35 Cal.3d 312 [197 Cal.Rptr. 581]..... 11

Ernst v. Cummings (1880) 55 Cal. 179..... 15

Estate of Buchanan (1954) 123 Cal.App.2d 546 [123 Cal.Rptr. 546, 267 P.2d 73]..... 17

Estate of Hermon (1995) 39 Cal.App.4th 1525 [46 Cal.Rptr. 577]..... 9

Hobbs v. Weiss (1999) 199 Daily Journal D.A.R. 6583 19

Kaufman, Appellate Advocacy in the Federal Courts (1977) 79 F.R.D. 165 19

McDorman v. Moody (1942) 50 Cal.App.2d 136 [122 P.2d 639]..... 16

Mediterranean Co. v. State Farm Fire & Casualty Company (1998) 66 Cal.App.4th 257 [77 Cal. Rptr. 781] 19

Moncharsh v. Heily & Blase (1992) 3 Cal.4th 1 [10 Cal.Rptr. 183, 832 P.2d 899].....11, 14

O'Malley v. Petroleum Maintenance Co. (1957) 48 Cal.2d 107 [308 P.2d 9] 14

Parsons v. Bristol Development Co. (1965) 62 Cal.2d 861 [44 Cal.Rptr. 767, 402 P.2d 829].....9, 10

Rubin v. Fuchs (1969) 1 Cal.3d 50 [81 Cal.Rptr. 373, 459 P.2d 925]..... 16

Stratton v. First National Life Ins. Co. (1989) 210 Cal.App.3d 1071 [258 Cal.Rptr. 721]..... 9

Statutes

Code of Civil Procedure

Section 166(a) 18
Section 657 18
Section 663 18
Section 664.6 18
Section 904.1(a) 8
Section 1003 18
Section 1005.5 18
Section 1280 10

* * *

APPENDIX V

Case No. _____

IN THE
SUPREME COURT OF THE STATE OF CALIFORNIA

FIRST PACIFIC BANK LIMITED, a Hong Kong Banking Corporation,	)
Plaintiff and Respondent,	)
v.	)
BENEDICTO V. YUJUICO, TERESITA M. YUJUICO, and THE BVY GROUP, INC.,	)
Defendants, Appellants and Petitioners.	)

After a Decision by the Court of Appeal, First Appellate District, Division Four
Case No. A091568

PETITION FOR REVIEW AND REQUEST FOR IMMEDIATE STAY

Gerald M. Murphy, Esq.
[State Bar No. 99994]
Michele A. Carli, Esq.
[State Bar. No. 140012]
JACOBS, SPOTSWOOD, CASPER & MURPHY, LLP
One Maritime Plaza, Suite 400
San Francisco, California 94111
Telephone No.: (415) 835-3700
Facsimile No.: (415) 835-1072

Attorneys for Defendants, Appellants and Petitioners
BENEDICTO V. YUJUICO, TERESITA M. YUJUICO, and THE BVY GROUP, INC.

TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES ii

I. ISSUE PRESENTED 1

II. WHY REVIEW SHOULD BE GRANTED 2

III. BACKGROUND AND STATEMENT OF FACTS 5

A. Stay Request 7

IV. LEGAL DISCUSSION 8

A. SUBSEQUENT DEVELOPMENTS IN STATE AND FEDERAL LAW SINCE THE *McCARROLL* DECISION WAS ISSUED NECESSITATE RECONSIDERATION BY THIS COURT 8

1. Subsequent Developments In Federal Law 8

2. Subsequent Developments In State Law 12

3. Petitioners' Request To Reconsider The *McCarroll* Decision May Properly Be Presented To This Court In The First Instance 13

V. CONCLUSION 14

TABLE OF AUTHORITIES

Page

Cases

Allied-Bruce Terminix Companies, Inc. and Terminix International Company v. Dobson (1995) 513 US 265, 130 L.Ed.2d 753, 115 S.Ct. 834 .....passim

ATSA of California v. Continental Ins. Co. (9th Cir. 1983) 702 F.2d 172..... 8

Auto Equity Sales, Inc. v. Super. Ct. (1962) 57 Cal.2d 450.....3, 14

Bauhinia Corp. v. China Nat. Machinery & Equipment (9th Cir. 1987) 819 F.2d 247..... 8

Charles J. Round Co. v. Joint Council of Teamsters (1971) 4 Cal.3d 888.....4, 13

Cloud v. Northrop Grumman Corp. (1998) 67 Cal.App.4th 995 4

Drake Bakeries v. Bakery Workers (1962) 370 U.S. 254, 8 L. Ed.2d 474, 82 S.Ct. 1346.....4, 15

Freeman & Mills, Inc. v. Belcher Oil Co. (1995) 11 Cal.4th 85..... 13

Keating v. Superior Court (1982) 31 Cal.3d 584 10

McCarroll v. L.A. County etc. Carpenters (1957) 49 Cal.2d 45.....passim

Moradi-Shalal v. Fireman's Fund Ins. Companies (1988) 46 Cal.3d 287, 292, fn. 1 14

People v. Birks (1998) 19 Cal.4th 108, 116, fn.6 .....4, 14

Peterson v. Super. Ct. (Banque Paribas) (1995) 10 Cal.4th 1185..... 13

TABLE OF AUTHORITIES
(cont.)

Page

Southland Corp. v. Keating (1984) 465 US 1, 79 L.Ed.2d 1, 104 S.CT. 852 ..... passim

Volt Information Sciences, Inc. v. Stanford Univ. (1989) 489 US 468, 103 L.Ed.2d 488, 109 S.Ct. 1248 11

Statutes

Code of Civil Procedure

Sections 1297.11-1297.432 3

Sections 1297.161-1297.166 ..... 4, 12

Section 1297.161 12

Section 1297.162 12

Section 1297.166 12

Section 31512 9

Title 9, United States Code

§§ 1 et seq 2

§ 2 ..... 8, 10

Rules

International Arbitration Rules of the American Arbitration Association

Article 3 12

Article 15.1 12

Article 15.3 12

* * *

APPENDIX VI

Case No. _____
[Related Case No. S089988]

IN THE

SUPREME COURT OF THE STATE OF CALIFORNIA

FIRST PACIFIC BANK LIMITED, a Hong Kong Banking Corporation,

Plaintiff and Respondent,

v.

BENEDICTO V. YUJUICO, TERESITA M. YUJUICO, and THE BVY GROUP, INC.,

Defendants, Appellants and Petitioners.

After a Decision by the Court of Appeal,
First Appellate District, Division Four
Case No. A085195

PETITION FOR REVIEW

Gerald M. Murphy, Esq.
[State Bar No. 99994]
Michele A. Carli, Esq.
[State Bar No. 140012]
JACOBS, SPOTSWOOD, CASPER & MURPHY, LLP
One Maritime Plaza, Suite 400
San Francisco, California 94111

Telephone No.: (415) 835-3700
Facsimile No.: (415) 835-1072

Attorneys for Defendants,
Appellants and Petitioners
BENEDICTO V. YUJUICO, TERESITA M. YUJUICO and THE BVY GROUP, INC.

TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES ii

I. ISSUE PRESENTED 1

II. WHY REVIEW SHOULD BE GRANTED 2

III. BACKGROUND AND STATEMENT OF FACTS 6

IV. LEGAL DISCUSSION 8

A. SUBSEQUENT DEVELOPMENTS IN STATE AND FEDERAL LAW SINCE THE *McCARROLL* DECISION WAS ISSUED NECESSITATE RECONSIDERATION BY THIS COURT 8

1. Subsequent Developments In Federal Law 8

2. Subsequent Developments In State Law 13

3. Petitioners' Request To Reconsider The *McCarroll* Decision May Properly Be Presented To This Court In The First Instance 15

V. CONCLUSION 16

TABLE OF AUTHORITIES

Page

Cases

Allied-Bruce Terminix Companies, Inc. and Terminix International Company v. Dobson (1995) 513 US 265, 130 L.Ed.2d 753, 115 S.Ct. 834 .....passim

ATSA of California v. Continental Ins. Co. (9th Cir. 1983) 702 F.2d 172..... 8

Auto Equity Sales, Inc. v. Super. Ct. (1962) 57 Cal.2d 450.....3, 15

Baker v. Sadick (1984) 162 Cal.App.3d 618 5

Bauhinia Corp. v. China Nat. Machinery & Equipment (9th Cir. 1987) 819 F.2d 247..... 8

Charles J. Round Co. v. Joint Council of Teamsters (1971) 4 Cal.3d 888.....4, 15

Cloud v. Northrop Grumman Corp. (1998) 67 Cal.App.4th 995 3

Drake Bakeries v. Bakery Workers (1962) 370 U.S. 254, 8 L. Ed.2d 474, 82 S.Ct. 1346.....4, 16

Freeman & Mills, Inc. v. Belcher Oil Co. (1995) 11 Cal.4th 85..... 14

Hawkins v. Superior Court (1979) 89 Cal.App.3d 413 5

Keating v. Superior Court (1982) 31 Cal.3d 584 9

Madden v. Kaiser Foundation Hospitals (1976) 17 Cal.3d 699..... 5

McCarroll v. L.A. County etc. Carpenters (1957) 49 Cal.2d 45.....passim

Moradi-Shalal v. Fireman's Fund Ins. Companies (1988) 46 Cal.3d 287, 292, fn. 1 15

TABLE OF AUTHORITIES

(Cont.)

People v. Birks (1998) 19 Cal.4th 108, 116, fn. 6 ....3, 15

Peterson v. Super. Ct. (Banque Paribas) (1995) 10 Cal.4th 1185 14

Portland General Electric Company v. U.S. Bank Trust National Association (July 18, 2000) 2000 Daily Journal D.A.R. 7819 .....11, 12

Posner v. Grunwald-Marx, Inc. (1961) 56 Cal.2d 169 13

Raytheon Co. v. Rheem Manufacturing Co. (9th Cir. 1963) 322 F.2d 173..... 12

Southland Corp. v. Keating (1984) 465 US 1, 79 L.Ed.2d 1, 104 S.CT. 852.....passim

United Steelworkers v. American Mfg. Co. (1960) 363 U.S. 564, 80 S.Ct. 1343, 4 L.Ed.2d 1403..... 13

Volt Information Sciences, Inc. v. Stanford Univ. (1989) 489 US 468, 103 L.Ed.2d 488, 109 S.Ct. 1248 11

Statutes

Code of Civil Procedure

Sections 1297.11-1297.432..... 3

Sections 1297.161-1297.166.....4, 13

Section 1297.161 13

Section 1297.162 13

Section 1297.166 13

Section 31512..... 8

TABLE OF AUTHORITIES

(Cont.)

Title 9, United States Code

§§ 1, et seq. 2

§ 2 ..... 8, 10, 12

Rules

International Arbitration Rules of the American Arbitration Association

Article 3 13

Article 15.1 13

Article 15.3 14

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